



RICK SNYDER
GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF TREASURY
LANSING

R. KEVIN CLINTON
STATE TREASURER

NUMBERED LETTER 2014-1

DEFICIT ELIMINATION PLANS

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2014-1 This numbered letter repeals numbered letter 2012-1, and further clarifies when a deficit elimination plan is required and how to determine the amount of deficit to be eliminated. Significant changes since numbered letter 2012-1 include the calculation of current liabilities and certain situations where deferred inflows of resources minus taxes and special assessments receivable may offset the deficit.

The Glenn Steil State Revenue Sharing Act of 1971, Public Act 140 of 1971, Section 21(2), states that units of local government (local units) who end their fiscal year in a deficit condition shall formulate a deficit elimination plan (plan). Any assessment of a local unit's deficit condition should be made at the fund level of reporting, not at the government-wide level. The plan shall be filed with the Department of Treasury (Treasury) for evaluation and certification. Primary local units are responsible for filing the plans of discretely presented component units.

Determining a Deficit for Governmental Funds (Modified Accrual)

For all governmental funds (not proprietary funds, fiduciary funds, or discretely presented component units), a plan is necessary to eliminate most "unrestricted fund balance" deficits. For governmental funds other than the General Fund, if the "deferred inflows of resources minus taxes and special assessments receivable" is greater than the "unrestricted fund balance", no plan is necessary. Unrestricted fund balance is the sum of the Committed, Assigned, and Unassigned balances. An unrestricted fund balance deficit exists when the local unit does not have sufficient resources available to cover the deficit. This occurs when the sum of the Nonspendable and Restricted fund balances is greater than the total fund balance. Resources available to cover the deficit includes assets that are not restricted by federal, state, or local laws, regulatory authorities, bond covenants, contractual agreements, or other legal constraints. Therefore, when funds have a total fund balance surplus and an unrestricted fund balance deficit, sufficient unrestricted resources do not exist to eliminate the deficit.

Determining a Deficit for Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units (Full Accrual)

Various methods have been used to determine the amount of a deficit in a proprietary fund, fiduciary fund, or a discretely presented component unit. For purposes of uniformity among all units of local government, effective immediately, Treasury will define a deficit as stated below. Local units will be expected to apply the same test to determine if a deficit elimination plan is necessary.

Proprietary Fund, Fiduciary Fund, and Discretely Presented Component Unit Deficit Test

Step 1: Does the “unrestricted net position” or “total net position” have a deficit? If both are “no”, no plan is necessary. If one is “yes”, is the “deferred inflows of resources minus taxes and special assessments receivable” greater than either deficit? If “yes”, no plan is necessary. If “no”, proceed to Step 2.

Step 2: Calculate current assets minus current liabilities. For this calculation, current liabilities should not include the current portion of long-term obligations. If the answer is positive, no plan is necessary. If the answer is negative, proceed to Step 3.

Step 3: Compare A) the larger deficit between the “unrestricted net position” and the “total net position”, and B) current assets minus current liabilities.

Step 4: Submit a plan to eliminate the smaller deficit between A and B.

Example 1

Unrestricted Net Position = (430,000), Total Net Position = 1,800,000

Deferred Inflows of Resources minus Taxes and Special Assessments Receivable = 150,000

Current Assets = 75,000, Current Liabilities = 60,000

Step 1: Unrestricted Net Position has a deficit > Deferred Inflows of Resources minus Taxes and Special Assessments Receivable. Proceed to Step 2.

Step 2: $75,000 - 60,000 = 15,000$. Answer is positive. No plan is necessary.

Step 3: Not Applicable

Step 4: Not Applicable

Example 2

Unrestricted Net Position = (430,000), Total Net Position = 1,800,000

Deferred Inflows of Resources minus Taxes and Special Assessments Receivable = 150,000

Current Assets = 75,000, Current Liabilities = 510,000

Step 1: Unrestricted Net Position has a deficit > Deferred Inflows of Resources minus Taxes and Special Assessments Receivable. Proceed to Step 2.

Step 2: $75,000 - 510,000 = (435,000)$. Answer is negative. Proceed to Step 3

Step 3: A **(430,000)** or 1,800,000, B (435,000)

Step 4: A is a smaller deficit than B. Submit a plan to eliminate the (430,000) unrestricted net position deficit.

Example 3

Unrestricted Net Position = (430,000), Total Net Position = 1,800,000

Deferred Inflows of Resources minus Taxes and Special Assessments Receivable = 150,000

Current Assets = 75,000, Current Liabilities = 200,000

Step 1: Unrestricted Net Position has a deficit > Deferred Inflows of Resources minus Taxes and Special Assessments Receivable. Proceed to Step 2.

Step 2: $75,000 - 200,000 = (125,000)$. Answer is negative. Proceed to Step 3.

Step 3: A **(430,000)** or 1,800,000, B (125,000)

Step 4: B is a smaller deficit than A. Submit a plan to eliminate the (125,000) difference between current assets and current liabilities.

Example 4

Unrestricted Net Position = (430,000), Total Net Position = (1,500,000)

Deferred Inflows of Resources minus Taxes and Special Assessments Receivable = 150,000

Current Assets = 75,000, Current Liabilities = 510,000

Step 1: Unrestricted Net Position and Total Net Position have a deficit > Deferred Inflows of Resources minus Taxes and Special Assessments Receivable. Proceed to Step 2.

Step 2: $75,000 - 510,000 = (435,000)$. Answer is negative. Proceed to Step 3.

Step 3: A (430,000) or **(1,500,000)**, B (435,000)

Step 4: B is a smaller deficit than A. Submit a plan to eliminate the (435,000) difference between current assets and current liabilities.

Example 5

Unrestricted Net Position = (430,000), Total Net Position = (450,000)

Deferred Inflows of Resources minus Taxes and Special Assessments Receivable = 150,000

Current Assets = 75,000, Current Liabilities = 610,000

Step 1: Unrestricted Net Position and Total Net Position have a deficit > Deferred Inflows of Resources minus Taxes and Special Assessments Receivable. Proceed to Step 2.

Step 2: $75,000 - 610,000 = (535,000)$. Answer is negative. Proceed to Step 3.

Step 3: A (430,000) or **(450,000)**, B (535,000)

Step 4: A is a smaller deficit than B. Submit a plan to eliminate the (450,000) total net position deficit.

Example 6

Unrestricted Net Position = (470,000), Total Net Position = (450,000)

Deferred Inflows of Resources minus Taxes and Special Assessments Receivable = 150,000

Current Assets = 75,000, Current Liabilities = 610,000

Step 1: Unrestricted Net Position and Total Net Position have a deficit > Deferred Inflows of Resources minus Taxes and Special Assessments Receivable. Proceed to Step 2.

Step 2: $75,000 - 610,000 = (535,000)$. Answer is negative. Proceed to Step 3.

Step 3: A **(470,000)** or (450,000), B (535,000)

Step 4: A is a smaller deficit than B. Submit a plan to eliminate the (470,000) unrestricted net position deficit.

Example 7

Unrestricted Net Position = (130,000), Total Net Position = 1,800,000

Deferred Inflows of Resources minus Taxes and Special Assessments Receivable = 150,000

Current Assets = 55,000, Current Liabilities = 60,000

Step 1: Unrestricted Net Position has a deficit < Deferred Inflows of Resources minus Taxes and Special Assessments Receivable. No plan is necessary.

Step 2: Not Applicable

Step 3: Not Applicable

Step 4: Not Applicable

Local units whose only deficit is for a proprietary fund, fiduciary fund, or discretely presented component unit where it has been determined a plan is not necessary should select “Yes” to question #2 on their Auditing Procedures Report (Form 496).

Filing Requirements

It is the position of Treasury that a reasonable plan to eliminate a deficit condition is vital to the fiscal well-being of a local unit as is early implementation of that plan. Therefore, local units should not wait until Treasury sends a request letter for a deficit elimination plan to develop one. By providing better guidance on what constitutes a deficit, it is the expectation of Treasury that a local unit will submit a plan as soon as possible after the close of its fiscal year end. A plan should be filed prior to or concurrent with the submission of the local unit’s audit report to Treasury.

A plan generally should be for one year, but in no case longer than five years. Local units with multiple year plans that do not meet their subsequent year deficit projections must submit a revised plan that adheres to the time frame that was originally certified, not to exceed five years. The continued certification of a plan may be contingent on the filing of monthly or quarterly update reports with Treasury, as deemed necessary. Plans and acceptable evidence (defined below) can be emailed to Treas_MunicipalFinance@michigan.gov or to the postal address provided. If a plan has been sent via email, it is not necessary to also send a copy via postal mail.

Acceptable Evidence to Support a Plan

- Certified copies of board/council resolutions (describing funds and amounts) approving additional appropriations sufficient to eliminate the deficit and a copy of the journal entry that shows that the transfer has been made or a trial balance.
- Projected budget approved by the legislative body as evidenced by a certified resolution itemizing yearly revenues by source, expenditures/expenses by activity, and changes in the fund balance/retained earnings through the year of the deficit’s eventual elimination. There is a five-year limit for an approved plan; the plan must be amended if the deficit increases or the plan is not otherwise followed.

Failure to Submit an Acceptable Plan

Should a plan not voluntarily be submitted, Treasury will no longer “request” a plan. The local unit will be sent, via U.S. Postal Service, a Notice of Intent to Withhold State Payments. The local unit will have 30 days from the date of the notice to file a plan. Should a plan not be filed within 30 days, we will withhold 25% of the local unit’s State Incentive Payments or payments issued under Public Act 140 of 1971, the Glenn Steil State Revenue Sharing Act of 1971. Once withheld, payments are released not when a plan has been filed, but when a plan has been evaluated and certified by Treasury.

If you have any questions, please contact our office.

Michigan Department of Treasury
Local Audit and Finance Division
P.O. Box 30728
Lansing, MI 48909
517-373-3227